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Arizona Corporation Commission

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Jane L. Rodda
Administrative Law Judge
Hearing Division
Arizona Corporation Commission
400 W. Congress
Tucson, AZ 85701-1347

Re: *Southwest Transmission Cooperative, Inc.'s ("SWTC" or the "Cooperative")
Reply to the Staff Response Dated November 30, 2006 ("Response"); SWTC
Construction Work Plan Finance Application; Docket No. E-04100A-06-0058*

Dear Judge Rodda:

SWTC submits this reply to the Staff Response on the Cooperative's Application to borrow \$49.575 million to finance its 2005-2008 Construction Work Plan ("CWP Application"). The Rural Utilities Service ("RUS") has approved SWTC's loan application. SWTC would request that the Commission also approve the CWP Application at its January 2007 Open Meeting so that construction of these necessary projects can move forward.

The Staff Response recommends that SWTC be authorized to issue long-term debt to the RUS/FFB in the amount requested in the CWP Application, i.e., \$49.575 million. However, Staff asks that the Commission approve that borrowing "subject to the condition that [SWTC] adopt an equity accumulation plan to build equity to at least 30 percent of total capital by the year 2015." (Response, p. 5.) The Commission has rejected that Staff recommendation three times in the past 16 months and the Cooperative asks that it do so again.

As the Administrative Law Judge is aware, Staff first made the 30% equity requirement recommendation in last year's rate case. SWTC opposed it. In Decision No. 68072 dated August 17, 2005, after discussing the evidence offered by Staff and the Cooperative in Finding Nos. 30-39, the Commission did not accept Staff's recommendation, instead finding as follows:

We do not adopt a requirement now, or do we read Decision No. 64227 as requiring, that SWTC achieve any specific equity goal. We do adopt the rates herein with the expectation that SWTC will be able to build much needed equity.

Jane L. Rodda
Administrative Law Judge
December 13, 2006
Page 2

Because we are requiring SWTC to file another rate case in no more than five years, in any case, adopting an ultimate goal of 30 percent at this time is not necessary.

(Decision No. 68072, p. 9, ll. 7-11.) (Emphasis supplied.)

The Decision did require SWTC to file an update of its December 2002 equity analysis with more current assumptions. The Cooperative did so on June 15, 2006. In the rate decision, SWTC also proposed and the Commission approved phased rate increases for 2006 and 2007 specifically aimed, among other things, at improving its equity position and supporting “future capital projects” such as the ones involved in this CWP Application. (Decision No. 68072, Finding 18.)

Staff again proposed its 30% equity contingency in Docket No. E-04100A-05-0151—an SWTC request for financing for the Sandario Substation Project:

SWTC asserts that Staff’s recommendation to adhere to a plan to increase equity to 30 percent of equity no later than 2015 is inconsistent with the findings in Decision No. 68702. In the recent rate case, the Commission did not require adherence to a capital plan to increase equity to 30 percent of total capital. Rather, Decision No. 68072 did not adopt any particular equity goal, but required SWTC to file an equity improvement plan...

(Decision No. 68179 dated September 30, 2005, Finding 17.) (Emphasis supplied.)

Finally, on February 23, 2006—another finance request—the Commission again rejected Staff’s recommendation to require the Cooperative to adhere “to a plan to increase equity as a percentage of total capital to 30 percent no later than the end of 2015”:

Because Decision No. 68072 requires SWTC to file another rate case no later than August 17, 2010, adopting an ultimate goal of 30 percent equity at this time is not necessary. We adopted rates in Decision No. 68072 with the expectation that SWTC will be able to build much needed equity, and placed restrictions on SWTC’s patronage refunds based on equity levels.

(Decision No. 68490, Finding 20.) (Emphasis supplied.)

With the rate increase which the Commission approved last year and the phased rate increases which have either taken effect or will take effect next year, SWTC has resumed its plan of gradually increasing equity which had been interrupted by the unanticipated loss of MW&E

Jane L. Rodda
Administrative Law Judge
December 13, 2006
Page 3

firm and non-firm transmission revenues.¹ Based on the assumptions stated in the Equity Analysis filed a few months ago, Staff's condition of 30% equity by 2015 would require almost 30% in rate increases in the next five years²—rate levels which simply are unnecessary to service current debt, finance capital projects like those in the CWP Application and maintain the Cooperative's financial integrity.

Staff also recommends—without any analysis as to why—that the Commission deny the Cooperative's request for authorization to change the specific projects within the CWP over its four- to five-year time frame without filing an application so long as the total amount borrowed does not exceed \$49.575 million. SWTC will not repeat here the reasons justifying this request which were discussed in the Application and at page 5 of the SWTC October 17, 2006 response to the initial Staff report. Recently, the Commission has several times indicated its willingness to consider more efficient and expedited regulatory methods where cooperatives are involved. As explained in the Application and initial response, this request has several regulatory safeguards and is tailored to meet those objectives.

The Cooperative requests that the Commission approve at its January Open Meeting RUS/FFB long-term financing in an amount not to exceed \$49.575 million for its 2005-2008 Construction Work Plan, as the same may be amended by SWTC. In that regard, SWTC also suggests a condition requiring it to file with the Director, Utilities Division a copy of any future CWP Amendment request at the same time the request is submitted to RUS for its review and approval. Your assistance in relation to this matter is appreciated.

Very truly yours,

GALLAGHER & KENNEDY, P.A.



By:

Michael M. Grant

MMG/plp
15169-8/1488045

¹ Staff's pro forma capital structure assumption with only 0.8% equity assumes full, immediate borrowing of the \$49.575 million. Instead, amounts will be borrowed gradually over the next three to four years. Positive margins will be achieved and equity will improve as the CWP is carried out.

² June 15, 2006 Equity Improvement Analysis, p. 3, final paragraph.

Jane L. Rodda
Administrative Law Judge
December 13, 2006
Page 4

Original and 13 copies filed with Docket
Control this 13th day of December, 2006.

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